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SUBJECT: U.S. INSURANCE GIANT ADVOCATES MULTINATIONAL APPROACH TO PRESSING CHINA ON MARKET ACCESS

CHENGDU 00000020 001.2 OF 002

¶1. (U) This message contains company proprietary information. Not for Internet distribution.

¶2. (SBU) Summary. U.S. insurance giant Liberty Mutual chose to open its first PRC branch (and later subsidiary) in southwest China's Chongqing, rather than enter the bruising Shanghai market like many other foreign insurers. Chinese law discriminates against foreign insurers by 1) blocking acquisitions of other insurance companies; 2) requiring consecutive applications to open successive branches, usually with a wait of at least one year; and 3) not allowing them to write mandatory, third-party auto insurance, the most profitable part of the business. China protects its domestic market to give it more time to develop; foreign firms are stronger in claims/risk research, and enjoy stronger brand images. Liberty Mutual has endured years of losses, and advocates that foreign governments and insurers "band together" to convince the Chinese government to promise a 10-year plan for market liberalization. End Summary.

Major U.S. Insurance Company Targets Southwest China

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¶3. (U) Liberty Mutual -- the fifth-largest property and casualty (P&C) insurance company in the United States -- first entered the China insurance market in 1993, its China subsidiary CEO Jackson Tang told Consul General recently. Liberty Mutual chose to open a branch to sell P&C insurance in Chongqing rather than Shanghai, where there were "too many P&C companies already." In 2007, Liberty Mutual converted its Chongqing branch office into a wholly owned subsidiary, mainly to take advantage of lower capital requirements for subsidiaries (RMB 20 million) versus branches (RMB 100 million). There are 18 local, Chinese insurance companies in Chongqing; New York-based MetLife also has a 50-50 joint venture (JV) there. (Note: Foreign life insurance companies must be JVs, Tang explained, while P&C insurance companies can be wholly owned. End Note.)

Three Ways China Unfair to Foreign Insurance Companies

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¶4. (SBU) Tang complained that Chinese law discriminated against foreign insurance companies in three ways:

1) Draft regulations that currently govern the insurance market do not allow foreign insurance companies to have two separate legal entities. This means, for example, that foreign insurance companies are not allowed to buy other insurance companies in the same line of business.

2) Foreign insurers must apply consecutively to open each new branch. Approval of each new branch usually takes at least one year. Expanding its operations beyond Chongqing, Liberty Mutual received approval in 2009 for a branch office in Beijing, and is now in the process of applying for a branch in Hangzhou.

3) Foreign insurers are not allowed to write mandatory, third-party liability auto insurance. Instead, they are only left with the least profitable parts of the auto insurance business -- physical damage and excess third-party insurance. Auto insurance currently accounts for 70 percent of China's total insurance market. Physical damage is the "worst part" of the auto insurance market because China has no deductibles -- a customer could run up operating costs, for example, by presenting a claim for one USD. Moreover, in order to sell excess third-party insurance, Liberty Mutual is forced to work with local insurance companies that sell mandatory third-party insurance since no customer buys only excess insurance. This means that local Chinese insurance companies are taking the "good part of the business even though Liberty Mutual finds them

the customers." (Note: Tang also asserted that China had, so far, failed to honor a WTO commitment to open up the mandatory third-party auto insurance business to foreign insurance companies. This issue was being addressed by both governments in the frameworks of the Joint Commission on Commerce and Trade (JCCT) and Strategic and Economic Dialogue (SED), he added. End Note.)

Beijing Protects Immature Insurance Market;

Central and Provincial Regulators Also a Macro-Barrier

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¶5. (SBU) Beijing maintains these protectionist measures because it believes the Chinese insurance market remains immature, and wants to give local insurers more time to develop, Tang said. Market opening will be "gradual, and years in the making," he predicted. Another "macro-barrier" to market access is how China has both the central government regulator in Beijing (the China Insurance Regulatory Commission), as well as insurance, banking, and stock market regulators in the provinces, Tang asserted. At the same time, he added, this macro barrier has been less of an issue for Liberty Mutual because it has maintained good relations with Beijing regulators, and the local Chongqing government.

Liberty Mutual Stronger Than Local Competitors ...

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¶6. (SBU) Liberty Mutual is much stronger than local P&C insurers, Tang confided, which tend to be weak in claims/risk research. Local insurers are jealous of Liberty Mutual, which enjoys a high industry ranking, good relations with regulators, and a strong brand image. Chinese customers tend to believe that foreign insurers are more reliable and provide better service. Liberty Mutual is already the sixth largest of 18 competitors in Chongqing (as well as the sixth largest of 17 foreign P&C companies in all of China), he noted.

... But Has Suffered Years of Losses

¶7. (SBU) Despite this growth, Tang explained, Liberty Mutual's China business is still not profitable because it does not have sufficient scale and, most importantly, because it lacks access to the market for mandatory, third-party auto insurance. He recounted how his head office in the United States gives him grief about continuing losses, forcing him to provide assurances that one day the company's China operations will be very profitable.

Foreign Governments/Insurers Need

Unity to Pressure for Market Access

¶8. (SBU) So far, more foreign insurance companies want to enter the China market than exit it, Tang said. This higher enter-exit proportion will continue as long as the (loss-making) foreign insurers continue to have a "wait and see" attitude toward whether the PRC will grant further market access. Tang claimed that foreign governments and companies have been too fractured in their approach to lobbying China on market access ("a plate of sand"). He advocated that foreign governments, insurers, and banks "band together" to convince Beijing to promulgate, for example, a "10-year plan" for liberalization. In the meantime, he stressed, Liberty Mutual would be ready to "eat 10 years of losses."
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